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Federal Communications Commission
Office of Secretary

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of:	)	CCBPol 97-4
	)	CC Docket No. 96-98
Petition of MCI for	)	
Declaratory Ruling	)	
	)	

Comments of LCI International Telecom Corp.

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Overview of Comments

The ILEC strategy of demanding the acquisition of third party licenses for intellectual property imbedded in a network element as a prerequisite of access to that element threatens to harm all potential LEC competitors in two ways: (i) Unless curbed, the practice will delay access to unbundled network elements by months or years, not weeks; (ii) The practice is certain to introduce the very discrimination in pricing to CLECs for unbundled elements that Congress set out to avoid in the 1996 Act, which will hit hardest those CLECs who, as relative newcomers to the general field of telecommunications, have yet to develop substantial intellectual property portfolios with which to bargain.

In the best of circumstances, the negotiation of an intellectual property agreement takes time. Here, competing LECs ("CLECs") are at the mercy of however many vendors the incumbent LECs ("ILECs") are prepared to name—literally dozens in the case of Southwestern Bell. Moreover, the problem is compounded because the ILECs control the information needed to ascertain whether third party intellectual property rights are in fact even implicated by CLEC access to unbundled network elements. With sole access to the relevant data, the ILECs have both the incentive and the *ability* to see issues where none exist. As the Commission has noted, there are sound reasons to be more than skeptical of the ILECs' contentions on this issue.

The response to the ILEC strategy should be two-fold. First, the Commission should rule that third party intellectual property rights generally are not implicated by CLEC access to unbundled network elements. An ILEC should be required to prove by clear and convincing evidence the basis for any deviation from that general rule. Second, in the event an ILEC proves that

a third party's rights are implicated by a request for access to a particular element, the incumbent LEC should be required to obtain a license extension so that the requesting CLEC may have access to the element on non-discriminatory terms. As a corollary of that requirement, ILECs should be ordered pro-actively to identify any potential third party licensing impediment to the provision of providing access to network elements on an unbundled basis and to enter into any necessary agreements to remove such impediments. An incumbent LEC should not be deemed to have met its obligations to provide access to unbundled network elements on a non-discriminatory basis under section 251 until the ILEC has obtained all such required license extensions.

Discussion

I. Requiring CLECs to Negotiate Third Party Licenses Is Unnecessary.

As the Commission noted in the August 8 Order, the ILECs raised third party licensing as an issue in connection with the unbundling of network elements but not in connection with the resale of local exchange services using those same elements. [See *First Report and Order, released August 8, 1996*, ¶ 419] That inconsistency of position illustrates why the claim that third party rights are threatened should be discounted, and ultimately rejected.

The resale of local exchange services under the 1996 Act and the August 8 Order involves an ILEC making its existing package of facilities and exchange services available to CLECs at a wholesale price (i.e., the LEC price less expenses incurred for marketing and other indirect items) for resale to CLEC customers. In a resale situation, the CLEC does not purchase the facilities or control them in any physical sense. With respect to intellectual property embedded in the ILEC's

local switching facilities, as an example, reselling CLECs stand in the same shoes as other customers of the ILEC and therefore need no direct license from any third party vendors.

The situation from a licensing standpoint should not materially differ for unbundled network elements. By making a network element available generically, rather than as a finished service package, an ILEC does not thereby put itself in a position of needing to sublicense technology to the requesting CLEC. The "concept of [unbundling] network elements . . . does not alter the ILEC's physical control or ability and duty to repair and maintain network elements." [*First Report and Order, released August 8, 1996*, ¶ 250] As with the resale of exchange services, by unbundling network elements, an ILEC will continue to sell access to facilities that it owns and controls. The differences will lie in the freedom that CLECs will have to compete by combining unbundled elements with features that the ILEC does not offer or in making other adjustments to the total service package offered to the end user. Those differences are indispensable to open the local exchange market to competition, but they should not affect the rights of third party vendors whose technology is imbedded in an unbundled element.

The 1996 Act's requirement that the price of access to an unbundled element reflect the true cost of providing the element will assure that CLECs pay their appropriate share of the ILEC's costs of third party technology embedded in an unbundled element. Lump sum royalty payments for technology imbedded in an unbundled element may be recovered through depreciation, and usage-based royalty payments may be recovered through operating expense adjustments. Either way, both the ILEC's and the third party vendor's interests can be protected.

II. Requiring CLECs to Negotiate Third Party Licenses Would Stifle Unbundled Element-Based Competition.

A. Delayed Access.

As illustrated by AT&T's experience with Southwestern Bell, at least some ILECs are prepared to require CLECs to obtain permission or license extensions from dozens of third parties as a condition of accessing unbundled elements. The effort required to reach agreement with any one of those vendors is likely to be substantial. Even though they have no legitimate claim, third parties so named by an ILEC have no incentive to acknowledge that their rights are unaffected by the provision of access to an unbundled network element. Regardless of the strength or weakness of a third party's claim, the mere fact that the ILEC has required the third party's permission would give the third party leverage to demand at least nuisance payment. Some vendors, moreover, are likely to demand payment measured by use as opposed to a single lump sum. The back and forth to establish the agreed amount and the method of measurement unavoidably will take time.

Negotiation of 72 license extensions, or any similarly large number of licences, cannot proceed simultaneously. No telecommunications carrier has a legal staff large enough simultaneously to carry on negotiations on that many contracts with dozens of separate companies (and no ILEC had to do so). Smaller CLECs, in particular, would be hard pressed to find the resources to move through the process in any way other than sequentially. In short, the practice of requiring CLECs to negotiate separately with third parties as a prerequisite to accessing unbundled elements is a highly effective way of delaying such access. As the Commission has found, the ILECs have every incentive to exploit such an opportunity. *First Report and Order, released August*

8, 1996, ¶ 307 ("We are also cognizant of the fact that ILECs have the incentive and the ability to engage in many kinds of discrimination. For example, ILECs could potentially delay providing access to unbundled network elements").

B. Discriminatory Access.

The process of requiring CLECs to negotiate individually for license extensions from vendors of intellectual property imbedded in network elements will lead unavoidably to price discrimination in access to those elements. The price of access will be disparate between the incumbent and entering competitors and among the entering competitors inter se.

Third party vendors can be expected to demand higher licensing prices from CLECs than from an ILEC because CLECs would enter the negotiations with constraints that the incumbent did not face. When making the initial decision whether to acquire and incorporate a particular piece of software or other technology into a network element, ILECs in most circumstances were at liberty to choose (i) whether or not to incorporate the technology, and (ii) where more than one technology was available for the same purpose, which of the available technologies to incorporate. The vendor whose technology was selected by the ILEC negotiates a second time with the CLEC free of those competitive constraints. If the CLEC is to have access to the network element in question, it must take the element with the technology choice that the incumbent has made. A rational, self-interested vendor in such circumstances will bid up the price of the technology it controls.

Some entrenched third party vendors may have other incentives to bid up the price to CLECs of technology imbedded in an ILEC's network elements. Indeed, some third parties may prefer not to have CLECs use unbundled elements at all. By raising the cost of such usage to CLECs, vendors

would increase pressure on CLECs to replicate the elements to which they seek access. From a third party's point of view, selling a new switch is likely to be far more attractive than obtaining royalties for use of a switch already sold.

The newer and smaller CLECs will be particularly vulnerable to the bargaining strength enjoyed by entrenched third party vendors. As newcomers to the telecommunications field, smaller carriers do not have the substantial portfolios of patents, copyrights and other intellectual property interests owned by older, more established telecommunications companies. Consequently, in licensing negotiations, smaller carriers would not have the leverage that comes with potential intellectual property claims against the opposing side. The absence of that leverage will put upward pressure on the prices third parties demand from smaller carriers.

III. Bargaining with Third Parties Should Be Left with the ILECs.

From the ILECs' point of view, the tactic of requiring CLECs to negotiate directly with third party vendors is an effective and costless way to delay making network elements available on an unbundled basis and to drive up the price to the CLECs of those elements. The tactic has that potential precisely because the ILECs and the regulators are not involved in such negotiaions in any direct way. An effective solution will require involving the ILECs and the oversight process under sections 251 and 252.

As noted, ILECs control access to the licensing agreements that underlie their assertion that negotiations with third parties are necessary. When faced with a similar disparity in access to information about incremental element costs, the Commission placed the burden of proof on the ILECs. [See *First Report and Order, released August 8, 1996*, ¶ 680 ("We note that ILECs have

greater access to the cost information necessary to calculate the incremental cost of the unbundled elements of the network. Given this asymmetric access to cost data, we find that ILECs must prove to the state commission the nature and magnitude of any forward-looking cost that it seeks to recover in the prices of interconnection and unbundled network elements.")] A similar burden should apply here. Any ILEC contending that it may not provide access to unbundled elements without permission from third parties should bear a burden of prompt disclosure and proof of the basis of the contention. Specifically, the ILEC should be required to disclose to the state commission and to any affected CLEC the identity of the third party in question, the nature of the third party's interests giving rise to the ILEC's concern, and the license, agreement or other documentation containing or underlying the third party's interests. On a related note, ILECs should be forbidden to enter any confidentiality agreement that would interfere with the discharge of the ILEC's duty of prompt and complete disclosure.

In addition to the burden of disclosure, the burden to negotiate and obtain any necessary third party permission should be placed on the ILEC rather than on the requesting CLECs. Thus, as an illustration, if a license extension from a third party were required as a condition of access to an unbundled element, the ILEC itself should be obligated promptly to obtain the required license extension from the third party. In negotiating any such license extension, the ILEC should be required to assure that it retains the ability to provide the element to itself and to the CLEC on *equal, non-discriminatory terms.* Anything less would permit the ILECs to avoid their obligations under section 251:

> The duty to provide unbundled network elements on "terms, and conditions that are just, reasonable, and nondiscriminatory" means, at a minimum, that whatever those terms and conditions are, they must be offered equally to all requesting carriers, and where applicable, *they must be equal to the terms and conditions under which the incumbent LEC provisions such elements to itself.*

[*First Report and Order, released August 8, 1996*, ¶ 315 (emphasis supplied)]

Placing the burden of negotiating with third parties for any required license extension on the ILECs should reduce the incentive to identify affected third party rights as a means of delaying access to unbundled network elements, but it will not eliminate altogether the ILEC's ability to impose delay. Dragging out the negotiation process also would have that effect. Consequently, in addition to placing the burden of negotiation on the ILECs, the Commission should impose at least some limits on the negotiation process itself. First, as for any new technology yet to be incorporated into a network element, ILECs should be required to ensure by agreement with any affected third party that, going forward, the ILEC and requesting CLECs will have unbundled access to the embedded technology on equal terms. Second, in the case of existing technology, ILECs should be required immediately to commence identifying and eliminating any alleged third party claim that would prevent the ILEC from providing unbundled access to any network element defined by the Commission (or as further sub-defined at the state level) on terms equivalent to the terms that apply to usage of the element by the ILEC. The Commission should rule that eliminating any third party claim that would impede access by CLECs to unbundled elements is an explicit component of the ILEC's duty under section 252(c)(3) to make unbundled network elements available to any requesting carrier on terms that are just, reasonable and nondiscriminatory.

Requiring an ILEC to negotiate with third parties to remove any hypothetical claims of third parties arising from unbundled access to network elements will promote the opening of local exchange markets to competitive forces in at least one other way. If a requesting CLEC were required to obtain license extensions from third parties, as Southwestern Bell insisted of AT&T, the CLEC would face costs of access to an unbundled element that the ILEC did not and never will incur. That follows from the fact that the ILEC would pay once for the imbedded technology in a network element and the CLEC would pay twice: first to the ILEC, which passes on to the CLEC part of the ILEC's cost of the embedded technology (in the form of access charges); and a second time to the third party (in the form of royalties or similar compensation for a license extension). Under that scenario, not only would the CLEC pay a cost the ILEC did not incur, but the CLEC's contribution to the ILEC's costs of the unbundled element would reduce the ILEC's own costs, thereby aggravating the cost disparity. By requiring an ILEC to negotiate any required license extension, the cost disparity will be eliminated because the ILEC will remain the only source of direct payment to the third party (with the CLEC contributing an appropriate portion to the ILEC of those incurred costs).

In the event that the Commission were not to place the burden of negotiation on the ILECs, some mechanism to ensure that CLECs do not pay twice for imbedded technology must be adopted. If not required to address third party claims itself, the ILEC should be required at a minimum to disclose with particularity the portion of the access charges it seeks that are attributable to payments to third parties for imbedded technology. Moreover, to the extent a CLEC is required to pay a third party vendor for a license extension or supplemental use agreement, the ILEC's costs related to that

same technology should not be included in the computation of the access charge to the CLEC for the network element in which the technology is imbedded.

Summary of Relief Requested

LCI encourages the Commission to rule that:

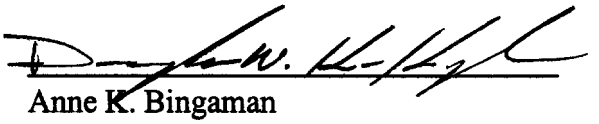
a. In general, providing access to unbundled network elements does not affect the interests of third parties whose intellectual property may be incorporated into a given element. To the extent an ILEC claims otherwise, it must disclose to the state commission and any affected CLEC the identity of the third party, the nature of the potential claim and the license agreement or other document containing or underlying the potential claim. No ILEC may agree to keep such information confidential. Disclosures must be made within ten days of a CLEC's request for access to the network element in question.

b. An ILEC involved in any negotiations regarding access to unbundled network elements or any proceedings before a state commission relating to such access has an affirmative obligation to begin immediately to eliminate any third party claim described in part (a) by agreement or through other lawful means. All third party claims shall be eliminated no later than fifeteen days from the CLEC's request for access to the network element in question (unless the ILEC proves good cause why a specific extension should be granted).

c. An incumbent LEC has not complied with its duty under section 251(d)(3) of the Telecommunications Act of 1996 to make network elements available on just, reasonable and non-discriminatory terms unless and until it has made the disclosures and removed the potential third party claims identified above.

April 14, 1997

Respectfully submitted,



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Certificate of Service

I, Patricia F. Garavito, certify that copies of the foregoing Comments of LCI International Telecom Corp. were sent by first class mail (or hand delivery, indicated by the *) to the following persons on April 15, 1997.

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